MONTANA

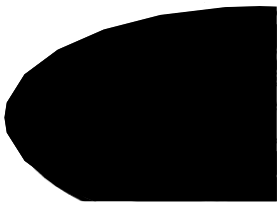
DRINKING WATER STATE REVOLVING FUND

ANNUAL REPORT

FOR STATE FISCAL YEAR 2001
(JULY 1, 2000 THROUGH JUNE 30, 2001)

Prepared by

Montana Department of Environmental Quality
and
Department of Natural Resources and Conservation



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MONTANA
DRINKING WATER STATE REVOLVING FUND (DWSRF)
ANNUAL REPORT
STATE FISCAL YEAR (SFY) 2001

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MONTANA
DRINKING WATER STATE REVOLVING FUND (DWSRF)
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I. INTRODUCTION

This Annual report adheres to the Operating Agreement negotiated between the State of Montana and the Environmental Protection Agency (EPA) concerning the administration of the Drinking Water State Revolving Fund (DWSRF). The annual report summarizes DWSRF activities for the state fiscal period beginning July 1, 2000 and ending June 30, 2001 (SFY01).

The DWSRF program was established as a result of the 1996 Amendments to the Federal Safe Drinking Water Act which provided the authority for EPA to make capitalization grants to states. The grants, in conjunction with state matching funds, are used to provide financial assistance for the construction of drinking water projects and to support administration of the state program.

In anticipation of the 1996 Amendments to the Federal Act, the 1995 State Legislature, under Title 75, Chapter 6, Part 2, Montana Code Annotated, passed the enabling legislation, entitled the Safe Drinking Water Treatment Revolving Fund Act, giving authority to the Montana Department of Environmental Quality (DEQ) and the Department of Natural Resources and Conservation (DNRC) to adopt administrative rules to implement the program. Legislation also provided ability to generate state match funds, through the sale of state General Obligation Bonds (GO Bond Authority). Amendments to the Drinking Water State Revolving Fund Act were passed in the 1997, 1999 and 2001 Legislative Sessions. The 1997 amendments changed the title of the Act from “Safe Drinking Water Treatment Revolving Fund Act” to the “Drinking Water State Revolving Fund Act” and also made other changes consistent with the Federal Act. During the 1999 Legislative Session, the 1999 amendment clarified the transfer language between the DWSRF and Water Pollution Control State Revolving Fund (WPCSRF) Programs and added GO Bond Authority. The 2001 Amendment authorized the program to advance funds to projects funded, in part, by the federal government when federal funding has been approved but not appropriated. This provides interim financing until those federal funds become available.

II. EXECUTIVE SUMMARY SFY01

During SFY01 Montana applied for and was awarded its fourth and fifth capitalization grant in the amount of $7,757,000 for FFY00 and $7,789,100 in FFY01.

Since the inception of the DWSRF, Montana has issued three GO bonds and one Bond Anticipation Note (BAN). The proceeds of which have been used as state match for loans, set asides, and program administration. Montana issued its first GO bond in October 1998 (SFY99), the second GO Bond in April 2000 (SFY00), and the third GO bond in June 2001 (SFY01). The total amount of bonds issued to date is $9,245,000. A summary of these bond issues is provided in Exhibit 1. Montana is planning for its fourth GO Bond in calendar year 2002.

Exhibit 1, Sources of DWSRF Funds Through SFY01, provide a complete tabulation of capitalization grant awards received through June 30, 2001, projected state match, binding commitments for loan projects through SFY01, and GO bonds and BANs issued for state match. The combination of capitalization grants and bond proceeds provide the needed funds for DWSRF projects, set asides, and program administration during SFY01. In addition, DNRC provided a portion of their program administration services as an in-kind contribution in the amount of $0.00 for SFY01.

During SFY01, the DWSRF program executed 10 project binding commitment agreements totaling $11,204,000, no increases were requested on any current or prior binding commitments. For a detailed breakdown of all DWSRF binding commitments signed and key dates of project activity that occurred in SFY01, refer to Exhibit 2: DWSRF SFY01 Binding Commitments Executed. See Exhibit 3 and 4 for the closed loans
Detailed information concerning use of DWSRF funds, accomplishments of the program and adherence with the stated goals of the program are provided on the following pages.

III. GOALS OF THE DWSRF

Long-Term Goals

1. To continue building and maintaining a permanent, self-sustaining state revolving fund program that will serve as a cost-effective, convenient source of financing for drinking water projects in Montana.

   Projects funded during SFY01 met all program requirements governing financial capability to assume debt. Ten of eleven communities received an interest rate of 4.0% on their loans (well below market rates) and one of the eleven qualified for an interest rate of 3.0% under the disadvantaged community criteria. These factors illustrate that the assistance is affordable, refer to Exhibit 3 & 4. A copy of the cash flow with all the activity through SFY01 is included in the report as Appendix A.

2. To provide a financing and technical assistance program to help public water supplies achieve and maintain compliance with federal and state drinking water laws and standards for the protection and enhancement of Montana's public drinking water.

   To promote the availability of these DWSRF program services during SFY01, DWSRF staff presented information at a variety of events. These included three infrastructure workshops, the annual Montana Rural Water Systems conference, the annual American Water Works Association/Montana Water Environment Association (AWWA/MWEA) conference, as well as meeting one on one with community leaders.

   Please also refer to the project descriptions and discussion of set-asides provided in Section V: Details of DWSRF Activity.

Short-Term Goals

1. Continue implementation and maintain the Drinking Water State Revolving Fund Program in Montana. Montana received approval of its DWSRF program and award of the FFY97 capitalization grant, June 30, 1998. Two additional capitalization grants were received during SFY00. These were the FFY98 Grant for $7,121,300 and the FFY99 Grant for $7,463,800. Two additional capitalization grants were also received during SFY 01. These

were the FFY00 Grant for $7,757,000 and the FFY01 Grant for $7,789,100.

2. Ensure the technical integrity of Drinking Water SRF projects through the review of planning, design plans and specifications, and construction activities.

   The trained technical staff of the Planning, Prevention and Assistance Division (PPAD) continue to use the DWSRF Handbook of Procedures and knowledge gained from eight years of operating the WPCSRF Program to ensure that this objective is met. The Handbook of Procedures is used as a guide to ensure that all state and federal laws governing the technical aspects of each project are satisfied.

   Steps were taken to update the Handbook of Procedures and streamline checklists and processes. This project was nearly completed during weekly sessions over most of the year utilizing the recommendations from EPA's annual review of the program. Other suggested improvements by program staff that have been noted during application to actual projects were also included in the revised handbook. A final revised edition was submitted to EPA in September, 2001.

   Staff attends training seminars and workshops to maintain and improve technical, financial and programmatic knowledge. In SFY01, Anna Miller, John Tubbs, Tom Livers and Mark Smith attended the Council of Infrastructure Financing Authorities (CIFA) National Workshop; Anna Miller, Mary Nichols, Jeff Lustgraaf, Marc Golz, Terry Campbell and Bob Fischer attended the DWSRF All States Workshop; Anna Miller attended the CIFA Legislative Conference; and Bob Fischer attended the annual Joint Engineers' Conference.

3. Ensure the financial integrity of the Drinking Water SRF program through the review of the financial impacts of the set-asides and disadvantaged subsidies and individual loan applications and the ability for repayment.

   See Appendix A: Cash Flow Model SFY01.

4. Ensure compliance with all pertinent federal, state, and local safe drinking water rules and regulations.

   To the best of our knowledge, the DWSRF program has ensured Public Water Supply Supervision (PWSS) compliance through the projects that have been funded and the various set-aside activities. Close coordination with the PWSS program has been essential in this effort.

5. Obtain maximum capitalization of the funds for the state in the shortest time possible while taking advantage of the provisions for disadvantaged communities and supporting the set-aside activities not directly related to the loan portfolio.

   Since the approval of its DWSRF loan program and first capitalization grant award, Montana has been awarded two more capitalization grants, utilized the provision to transfer funds between the WPCSRF and DWSRF, and generated other revenue from loan repayments and interest investments. The loan fund now totals over $43,179,000.

IV. FINANCIAL REPORTS

The Montana Legislative Audit Division (LAD) has completed their audit work of the SFY00 financial statements and presented their audit report to the Legislative Audit Committee (LAC) in June 2001, an unqualified opinion was issued for the financial statements. A copy of the report has been submitted to EPA Region VIII.

DEQ and DNRC engaged LAD to audit the State Revolving Fund financial activity beginning in SFY98. This decision was based on a new audit requirement conveyed in a directive from the Office of Water, Inspector General's Office, and the Office of Management and Budget. Prior to SFY98, LAD performed an annual review.

A copy of the SFY01 unaudited financial statements, including footnotes is attached as Appendix B of this report. The LAD has completed their audit of the SFY00 DWSRF activity. The SFY01 audit should be complete by June 2002.

V. DETAILS OF DWSRF ACTIVITY

A. LOAN ASSISTANCE

During SFY01 the DWSRF program closed eleven loans; signed ten project binding commitment agreements; and increased no binding commitments.

Project Bypass

If it is determined by DEQ that a project or projects are not ready to proceed or that the project sponsors have chosen not to use the Drinking Water SRF funds, other projects may be funded in an order different from that indicated on the priority list. If DEQ chooses to bypass higher ranked projects, it should follow the bypass procedure.

Montana bypassed 121 projects on its Priority List with the funding of River Rock, ranked 132. Ten other loans were closed. Refer to Exhibit 3: DWSRF Capitalized Grant Closed Loans For SFY01 and Exhibit 4: DWSRF Recycled Closed Loans For SFY01. The notification included the proposed projects to be funded, and the assurance that funds were still available for all loan applications anticipated at that time. All communities on the Priority List were notified in accordance with the above procedures, and no responses were received. No emergency projects were funded in SFY01.

Disadvantaged Communities

Communities seeking a Drinking Water SRF loan that meet the disadvantaged community criterion described in the Intended Use Plan may receive an additional subsidy on their SRF loans, beyond the standard below-market rate financing. This includes communities that will meet the disadvantaged criterion based on projected rates as a result of the project.

In SFY01, Montana closed one loan at a 3% interest rate, in the amount of $130,000, with one community that satisfied the disadvantaged criteria.

Small Systems
The table below shows the breakdown of the population served by our loans in FY01. We have 11 loans for a total of $11,292,701. Nine of these loans are with small systems that serve a population of less than 10,000 for a total of $7,531,701. This represents 67% of the loans made in FY01.

Public Water Supply	Population	Loan Amount
1. Cascade	725	$130,000
2. Colstrip	2600	$563,000
3. Conrad	2903	$650,000
4. Cut Bank II	3456	$576,000
5. Ennis	1017	$59,701
6. Fort Peck WD	744	$1,520,000
7. Great Falls	56,395	$3,000,000
8. Kalispell	16,089	$761,000
9. Lockwood	5400	$1,700,000
10. Missoula County Fairgrounds	100	$233,000
11. River Rock	347	$2,100,000
TOTAL		**$11,292,701**

Projects Provided Funding
Following is a brief summary of the projects which began or continued activity during SFY01:

The Town of Cascade Construction loan refinanced a new deep well into the Madison aquifer formation and the connecting piping to tie this source into the City water supply. All work was completed in late Spring of 2001. The City then submitted an application to the DWSRF to help refinance only a small portion of the total project cost. This project will help Montana meet its intended use plan goals of ensuring the City is able to meet both water quality and quantity requirements over the next 10 to 20 years. Funding this project addresses public health protection through compliance with the Total Coliform Rule. Historically, Cascade has experienced coliform bacteria problems associated with a spring source and has also abandoned one of the City's largest wells due to a leaking underground storage tank.

The City of Colstrip Construction loans (Phase I & II) funded design and construction of water main replacement work only. The existing water system was installed in the 1950's and much of the existing infrastructure needs to be replaced. Phase I construction work began in June 2001 and was completed in early September, 2001. Phase II design is complete with construction anticipated to occur in the Spring and Summer of 2002. Funding this project addresses public health protection through system maintenance to minimize leakage and potential cross connections.

The City of Conrad Construction loans (Phase I & II respectively) funded design and replacement of old filter under drain and backwash systems and installation of a new pre-treatment process (ballasted sedimentation). The Phase I project is complete at this time and the Phase II project is scheduled to begin construction in late Fall 2001. This project will help Montana meet its intended use plan goals of ensuring the City is able to meet both water quality and quantity requirements over the next 10 to 20 years. Funding this project addresses public

health protection through compliance with the surface water treatment rule. Historically, Conrad has had difficulty meeting turbidity requirements intermittently over the past couple of years. **The City of Cut Bank Construction loan** funded a new surface water treatment plant intake adjacent to the city's water treatment plant in Cut Bank Creek, along with sedimentation and flocculation process improvements to the existing water treatment plant. Also a new booster pump station was constructed to improve distribution pressure problems experienced by the City. Construction began in November 2000 and is mostly complete as of this narrative. Only finish work on the intake needs to be completed. The construction loan has not been closed. This project will help Montana meet its intended use plan goals of ensuring the City is able to meet both water quality and quantity requirements over the next 10 to 20 years. Funding this project addresses public health protection through compliance with the surface water treatment rule. Historically, Cut Bank has had difficulty meeting turbidity requirements and has been placed on Health Advisories and Boil Orders intermittently over the past couple of years.

The Town of Ennis loan was used to refinance an interim loan that had been made to the Town of Ennis by the Montana Board of Investments for the purpose of settling a claim associated with the Town's 1996 Water System Improvements Project. That project consisted of the construction of a new storage reservoir; a new 6,000 lineal foot transmission main; and the replacement of 60% of the existing distribution system. The amount of the Drinking Water State Revolving Fund Loan was $59,701; the refinance was completed in 2001.

The Fort Peck Rural Water District construction loan funds the construction of water system improvements to meet increased demand within the District boundaries. Existing individual groundwater supplies within this area do not meet drinking water quality standards. The project consists of the expansion of the Town of Fort Peck's water treatment plant, improvements to the town's transmission and storage facilities and the construction of a distribution system to serve the Fort Peck Rural Water District. The improvements include high service pumps, a transmission pipeline to the district's new water reservoir, distribution mains throughout the district service area, pump stations, pressure regulating stations, air release manholes, telemetry and system controls. The total loan amount is $1,520,000. Construction began in September 2000 and completion is expected in November 2001. This project helps Montana meet its intended use plan goals of ensuring the technical integrity of the project and funding a project that addresses public health protection by providing water to areas that meets water quality standards.

The City of Great Falls engineering and construction loan will fund four separate projects. One project will be an engineering study to update the City's Water Master Plan. A second project will be an engineering study to comprehensively evaluate the condition of, and make recommendations for improvements to, the distribution system storage reservoirs. A third project is to replace existing deteriorated water mains. A fourth part is to refinance a previous main replacement project. The authorized loan amount is $3,000,000 and the loan closed on December 21, 2000. Replacement of existing deteriorated mains is on going at this time. This project will help Montana meet its intended use plan goals by protecting public health through replacing leaking and deteriorated pipes, by helping the public water supply improve its technical and managerial capacity in updating its water master plan and proactively addressing the maintenance of its storage reservoirs.

The City of Kalispell loan is to finance the replacement of water mains. Two cast-iron water mains approximately 68 years old and in poor condition and predisposed to leaking have been replaced. This project helps Montana meets its intended use plan goals by proactively addressing distribution system problems in order to maintain public health protection and by

ensuring the technical integrity of the project.

Lockwood Water and Sewer District project consisted of purchasing an existing water system by the Water and Sewer District. The debt was purchased on May 1, 2001. Total funds drawn through June 30, 2001, were $1,700,000 of which $1,700,000 was drawn in SFY2001. This existing water system included a surface water intake, groundwater wells, treatment plant, storage reservoirs, and distribution system. The project has assisted the State of Montana in meeting its IUP goals by enabling the District to provide service to local users in compliance with drinking water standards and to increase the District's technical, financial and managerial capacity to maintain compliance. Public health is protected as a result of this project.

The Missoula County Fairgrounds engineering and construction loan provided funding to improve the distribution system of this small public water supply. The improvements were primarily to protect the potable water supply from many cross-connections within the system discovered by the Missoula City-County Health Department. The authorized loan amount was $233,000 and the loan closed on August 1, 2000. The project was completed in June of 2001. This project helps Montana meet its intended use plan goals by addressing public health protection through cross-connection control and backflow prevention and by ensuring the technical integrity of the project.

River Rock County Water and Sewer District project consisted of purchasing the debt of the Water and Sewer District. The debt was purchased on May 4, 2001. Total funds drawn through June 30, 2001, were $2,100,000 of which $2,100,000 was drawn in SFY2001. This project consisted of purchasing an existing water system that included two wells, a storage reservoir, a booster pumping station, and distribution system. The project has assisted the State of Montana in meeting its IUP goals by enabling the District to provide service to local users in compliance with drinking water standards and to increase the District's technical, financial and managerial capacity to maintain compliance. Public health is protected as a result of this project.

Summary of Loan Assistance:

A tabulation of aggregate information can be found in Exhibit 5, History of DWSRF Binding Commitments. This table tabulates the quarterly federal payments, totals quarterly SRF binding commitments and cumulative binding commitments, and calculates Montana's achievement of its 100% binding commitment grant condition. This fiscal year, the DWSRF maintained steady performance by executing project commitment agreements. The DWSRF completed SFY01 with binding commitments totaling 221% based on grant payments received four quarters earlier. We project in SFY02 that we will execute in excess of $5,715,212 in binding commitments. See Exhibit 6: DWSRF Projected Binding Commitments SFY02.

B. FIRST-ROUND FUNDED LOANS:

First-Round loans are financed with capitalization grants and state match. The DWSRF has financed the projects listed in Exhibit 3: DWSRF Capitalized Grant Closed Loans For SFY01.

C. RECYCLED FUNDED LOANS:

Recycled loans are financed with loan repayments from first round money and funds from transfers from the WPCSRF program the projects listed in Exhibit 4: Recycled Closed Loans For SFY01.

D. SOURCE OF FUNDS:

Two sources of funds are used to capitalize the DWSRF: (1) the Federal Capitalization Grant, which provides 80% of the DWSRF loan funds; and (2) the state match, funded through the sale of GO bonds, which provides 20% of the DWSRF loan funds. State legislation originally authorized the sale of up to $10 million in GO bonds to match federal grant funds. In the 1999 Legislative session an additional $10 million of GO bonds was authorized for state match bringing the total to $20 million. This amount is adequate to cover funds currently authorized for the program. At the time this report was written, $9,245,000 of GO bonds have been issued by the DWSRF program to use as state matching funds. See Exhibit 1: Sources of DWSRF Funds through SFY01. In-kind services of $0.00 have been provided to the DWSRF program by DNRC as match to federal grant funds and were used for program administration. Also, $8,782,486 of funds have been transferred from the WPCSRF to the DWSRF for loans. See Exhibit 7 for a breakdown of transferred funds.

E. FEDERAL FUNDS DRAWN BY THE PROGRAM:

Exhibit 8, SFY01 Summary of DWSRF Federal LOC-ACH Draws shows thirty-nine loan disbursement requests for $4,758,266, twelve administrative set-aside disbursement requests for $370,580 and ten non-administrative set-aside disbursement requests for $697,085 were made for a total of $5,825,931 drawn on the Federal Letter of Credit, Automatic Clearing House (LOC-ACH) during SFY01.

F. SET – ASIDES

DWSRF Budget and Draws by Set-Asides displays the financial summary of these non-project activities, see Exhibit 9.

Administration

The DWSRF set aside the maximum four percent from the capitalization grants for program administration. DEQ's contract with DNRC and other activities that occurred were:

- review and assistance during planning, design, project bidding and construction.
- loan origination work, administering repayments.
- preparation of bond issuance with state's bond counsel firm of Dorsey & Whitney.
- financial modeling.
- DWSRF program audit.
- costs associated with the legislatively appointed advisory committee.
- public comment processes.

Small Systems Technical Assistance Set-Aside

DEQ developed a Work Plan for a small systems technical assistance set-aside during the spring and summer of 1998. The Work Plan was submitted to EPA on September 1, 1998 and approved on November 12, 1998. As outlined in the Work Plan, DEQ developed a RFP to provide the technical assistance via a contractor. The DEQ received proposals from 8 different contractors.

The successful contractor, Midwest Assistance Program, was notified of acceptance of the

firm's proposal. The O&M contract has been in effect since May 1999 and nearly 300 site visits have been completed, providing both long and short term O&M assistance. These visits have been followed by more than 40 return trips and have been very popular and beneficial. Assistance provided under this contract has resulted in lifting boil orders at a couple of surface water treatment plants, greatly improved treatment performance at several others and development of long range O&M planning at many small systems. The technical assistance provider has provided assistance ranging from identifying physical problems with the water system equipment to providing a written guide for a record keeping system to assisting communities without certified operators acquire and train staff.

A written survey of systems was performed to evaluate the contract by DEQ DWSRF staff in June 2001 to determine if the contract should be continued. Twenty-two systems selected at random were contacted and asked to complete a simple check-box survey to evaluate the performance of the contractor. All of the systems contacted were positive about the service provided and several said they benefited and would not hesitate to call on the contractor again. Following are examples of the service being provided under this contract:

- helping operators to identify and prioritize water system needs
- helping operators to address the identified needs
- helping operators in discussions with boards, councils and other administrators when necessary
- helping operators & owners identify and isolate leakage problems resulting in pressure losses
- helping operators to operate and calibrate water treatment analytical and chemical feed equipment
- helping operators to repair malfunctioning analytical or chemical feed equipment
- explaining disinfection practices
- briefly discussing capacity development, cross-connections, source water protection, water conservation and operator certification requirements and providing the operator with a list of people or organizations to contact for in-depth information on these subjects

The contractor is also available to provide targeted technical assistance when the need arises. This service has been provided five times over the period from 7/1/00 to 6/30/01. As an example the contractor trained a new operator at a surface water treatment plant a small community was left with an unexpected retirement of the only operator. The result of the assistance in each of these cases was to help the systems back into compliance with drinking water standards, thus ending compliance cases. This contract allows DEQ to request that the contractor not only help make the initial adjustments, but also provide the operator with the necessary information to properly operate and maintain the equipment on his own.

PWSS Set-Aside: Administration

This set-aside funded salaries, benefits and operating expenses for two water quality specialists recently hired and assigned to the Billings and Kalispell Regional Offices, respectively. (In addition, four new FTE are being proposed for next year, which will require approval of a budget amendment through the legislative Executive Planning Process.) All of these positions provide direct assistance to water suppliers in implementation of the Lead and Copper Rule, the Phase 2/5 rules, the Total Coliform Rule, the Consumer Confidence Report Rule, the Interim Enhanced Surface Water Treatment Rule, and Stage I Disinfection/Disinfection By-Products Rule. The set-asides also funded database development expenses associated with implementation of SDWIS/state and associated state-specific Oracle modules.

PWSS Set-Aside: Source Water Protection (SWP)

The SWP Section at DEQ developed and submitted the workplan for this set-aside in the late fall/early winter of FY01. DEQ received notification of workplan approval by EPA in January 2001. Some work was performed under contracts to provide technical support to local communities that assisted in the development of Source Water Delineation and Assessment Reports. In addition, DEQ staff performed some source water protection training for PWS operators. But regrettably, DEQ was unable to complete accounting procedures necessary to fully utilize the funding for this set-aside in FY01. Full implementation of the activities under this set-aside are anticipated during this next fiscal year.

Capacity Development Set-Aside

The 1996 Amendments to the Safe Drinking Water Act allow states to use SRF funds to establish authority to enforce capacity requirements and to implement a capacity development strategy. This ensures that all new and existing community and non-transient non-community public water supply systems have the necessary technical, financial and managerial capability to comply with all of the primary requirements of the SDWA. EPA also requires that systems demonstrate adequate capacity in these areas as a condition of approval for Drinking Water SRF loans.

The state will lose substantial portions of successive capitalization grants if it does not develop and implement strategies to assist existing water systems with capacity development. The portions of the grants that may be lost are 10 percent in FY 2001, 15 percent in FY 2002, and 20 percent of each subsequent year's funds. DEQ avoided the first of these withholding provisions by obtaining approval in 2000 of the state's Capacity Development Strategy for Existing Public Water Supply Systems. Future withholding can be avoided by adhering to the approved strategy and complying with the requirements for reporting capacity development improvements to EPA.

The strategies are a methodology that will be used to identify and prioritize public water systems in need of improving technical, financial, and managerial capacity (a complete copy of the capacity development strategies can be obtained from DEQ). Part of these strategies include providing assistance to those systems by use of the set-aside funding. The state of Montana has over 1900 public water supplies. Given the large number of systems and a shortage of staff with the requisite financial and managerial experience, DEQ has chosen to provide these services through a contractor. A contract with the Midwest Assistance Program (MAP) was signed on March 2, 2001, to provide $100,000 of contracted services during the remainder of calendar year 2001. It is anticipated the contractor will provide in-depth financial and managerial assistance to a minimum of 25 public water supplies during the initial contract time period.

The format for financial and managerial assistance will begin with telephone or written contact with the selected water system followed by one or more on-site visits to evaluate the financial and managerial status of the system. Following the site visits, a written report will be prepared and mailed to the system owner or manager, summarizing the observations and

recommendations discussed during the evaluation. A copy of any written correspondence will also be forwarded to DEQ.

PWSS Set-Aside: Operator Certification

This set-aside has been used for personal services and operating expenses for staff in the Operator Certification Program. Set-aside funds are used to pay portions of the salary and benefits for all three full-time staff positions, as well as program operating expenses.

In the past year, the program has certified over 1500 public water system operators, including Operators for 638 community systems and 232 non-transient non-community systems. Certification program activities include public outreach, collection and processing of applications, collection and processing of examination and certification fees, training, administration of exams, monitoring of continuing education credits, compliance monitoring, and assistance with formal enforcement activities. Over 90% of the public water supply systems in each category have certified operators.

The Certification Program Manager sent the draft program to EPA Region VIII and Headquarters in October of 1999 to request approval of our Operator Certification Program. Positive feedback for the program was been received from both EPA Region VIII and Headquarters, and the program was been formally approved in December 2000.

The department requested and received approval for spending authority from the 2001 state legislature for very small water system expense reimbursement grant funding if that grant money should be obtained from EPA. The department also requested and received approval for another full-time operator certification staff person to administer this program.

The draft grant application for the small water system expense reimbursement grant funding was sent to EPA Region VIII on July 13, 2001. Comments were received from EPA Region VIII and Headquarters on October 3, 2001. The program is in the processing of responding to these questions and working with EPA at this time. If all goes according to plan, we hope to begin reimbursing funds July 1, 2002.

Local Assistance and Other State Programs – Source Water Delineation and Assessment

Montana used funds from this set-aside for delineation and assessment. The Montana SWP Program was submitted to EPA in January 1999, following an extensive development process that included advisory council input as well as consideration of comments received through public meetings held around the state and an Internet based enhanced public participation project. EPA approved the program in November 1999.

The Montana SWP Program uses a combination of approaches to complete the assessments. For many source waters, state staff resources will complete the source water delineation and assessment reports. For sources serving qualified community water systems, a pass through grant option is in place to allow a public water system (PWS) to complete the delineation and assessment report either directly, where in-house expertise exists, or through a contractor of their choice. The latter is a delegation mechanism intended to help develop local ownership of the effort as well as to help complete the reports by the statutory deadline. The process by which this delegation will occur and the criteria by which eligible communities will be selected is more fully described in the Montana SWP Program document.

A web-based *Source Water Protection Program Query Tool* was put on-line during the reporting period. This tool allows the user to identify and map selected contaminant sources within a specified distance of public water supply systems. The tool is intended to facilitate program implementation by DEQ staff as well as implementation by others through the pass through grant option.

VI. GRANT CONDITIONS AND CERTIFICATIONS

The State of Montana agreed to the following conditions outlined in the Operating Agreement. These items are discussed in more detail throughout the body of this report. To the best of our knowledge, DEQ and DNRC have abided by all requirements of state and federal law in the administration of this program.

(a) Assurance that the State has the authority to establish a Fund and operate the DWSRF program in accordance with SDWA.

The State of Montana's authority was re-certified and included with our applications for the FFY00 and FFY01 capitalization grants.

(b) Assurance that the State will comply with State Statutes and regulations.

(c) Assurance that the State has the technical capability to operate the program.

(d) Assurance that the State will accept capitalization grant funds in accordance with a payment schedule.

Please see Exhibit 8: DWSRF Projected vs. Actual Federal LOC-ACH Draws.

(e) Assurance that the State will deposit all capitalization grant funds in the Fund or Set-Aside Account.

(f) Assurance that the State will provide an amount equal to at least 20 percent of the capitalization grant (State match) in the Fund.

(g) Assurance that the State will deposit net bond proceeds, interest earnings, and repayments into the Fund.

(h) Assurance that the State will match capitalization grant funds the State uses for 1452(g)(2) set -asides.

(i) Assurance that the State will use Generally Accepted Accounting Principles.

(j) Assurance that the State will have the Fund and set-aside account audited annually in accordance with Generally Accepted Government Auditing Standards.

Please see Appendix B

(k) Assurance that the State will adopt policies and procedures to assure that borrowers have a dedicated source of revenue for repayments (or in the case of privately owned

system, demonstrate that there is adequate security).

(l) Assurance that the State will commit and expend funds as efficiently as possible, and in an expeditious and timely manner.

(m) Assurance that funds will be used in accordance with the Intended Use Plan.

(n) Assurance that the State will provide EPA with an Annual Report.

The submission of this document will fulfill the State of Montana's responsibility to submit a report.

(o) Assurance the State will comply with all Federal cross-cutting authorities.

(p) The state agrees that it will conduct an environmental review and a determination will be executed and distributed using a state process consisting of the same level of environmental detail required under the state Environmental Review Process for the Drinking Water SRF Program.

All construction projects that received assistance during SFY01 were reviewed and approved using the Montana Environmental Policy Act (MEPA). It was determined that no Environmental Impact Statements were necessary. An Environmental Assessment was prepared and a Finding of No Significant Impact was issued for all projects.

(q) The use of set-asides for Administrative Expenses, Small Systems Technical Assistance, State Program Management (Public Water Supply Supervision, Source Water Protection, Capacity Development, and Operator Certification), and Local Assistance and Other State Programs (Source Water Delineation) will be identified each year in the IUP and established in accordance with the Drinking Water SRF Program Guidelines.

(r) Specific Requirements under Title XIV

1. In accordance with Section 1420(a) of the Safe Drinking Water Act, the state has the authority to ensure that all new community water systems and new nontransient, noncommunity water systems commencing operation after October 1, 1999, can demonstrate technical, managerial, and financial capability with respect to each national primary drinking water regulation in effect.

   EPA has reviewed and approved Montana's capacity development authority and strategies. Administrative Rules that implement Montana's strategies became effective on September 10, 1999.

2. The state currently has a water and wastewater treatment plant operators certification program within the Permitting and Compliance Division, Department of Environmental Quality.

In addition, the following conditions were given with the Capitalization Grant Award. To the best of our knowledge, DEQ and DNRC have abided by these requirements as well.

- The recipient agrees to ensure that all space for conferences, meetings, conventions, or training funded in whole or in part with Federal funds complies with the Hotel and Motel Fire

and Safety Act of 1990.

- EPA Order 1000.25 Recycled Paper – DEQ is using recycled paper for printing reports to be delivered to EPA.

- Minority Business Enterprises/Women Business Enterprises (MBE/WBE) Utilization Under Federal Grants – During SFY01 loan recipients were required to comply with all Federal requirements concerning Disadvantaged Business Enterprises (DBE) Utilization either by project specification or submitting appropriate reports during construction.

- The state's fair share goal for DBE participation is 5% for SFY01 (2% MBE, 3% WBE). Refer to Exhibit 10 for the summary of the DWSRF Loans- MBE/WBE for contracts awarded during SFY01.

VII. CURRENT STATUS AND FUTURE ACTIVITIES

The DWSRF continues to use the US Bank as its trustee to manage funds and accounts established under the program. To date this arrangement has been very beneficial. DNRC gained access by computer modem to US Bank accounts which has made monthly reconciliation of WPCSRF and DWSRF accounts more timely. D.A. Davidson and Co. and Piper Jaffray Inc. continue to act as the DWSRF bond underwriters and financial advisors. Dorsey & Whitney will continue to act as DWSRF bond counsel for the general obligation bonds issued in future fiscal years.

Also, DEQ has begun work on the development of a complete database, which ultimatelywill include links with the DWSRF, the PWSS program, and fiscal services in both DEQ and DNRC The Planning Division has hired a .5 FTE position for development of the WPCSRF and DWSRF databases. This person is coordinating database development and serves as liaison between SRF program staff and DEQ's data processing staff. The target is to have the system fully operational by the start of the next state fiscal year, 2002, which also will facilitate federal reporting.

The following schedule indicates the key dates for continuation of the Drinking Water State Revolving Fund Loan Program in SFY02:

SFY02 ESTIMATED KEY DATES	ACTIVITY
July 2001	Held DWSRF bi-monthly meeting
September 2001	Held DWSRF bi-monthly meeting
October 2001	Held planning and financing workshops to promote and market DWSRF program
November 2001	Held DWSRF bi-monthly meeting
January 2002	Hold DWSRF bi-monthly meeting
Spring 2002	Hold infrastructure financing workshops to promote and market DWSRF program
March 2002	Hold DWSRF bi-monthly meeting

SFY02 ESTIMATED KEY DATES	ACTIVITY
May 2002	Hold DWSRF bi-monthly meeting
May 2002	Attend Region VIII all states meeting

VIII. GLOSSARY OF ACRONYMS AND INITIALIZATIONS

ACH	Automatic Clearing House
AWWA/MWEA	American Water Works Association/Montana Water Environment Association
BAN	Bond Anticipation Note
CIFA	Council of Infrastructure Financing Authorities
DBE	Disadvantaged Business Enterprises
DEQ	Montana Department of Environmental Quality
DNRC	Montana Department of Natural Resources and Conservation
DWSRF	Drinking Water State Revolving Fund
EPA	Environmental Protection Agency
FFY	Federal Fiscal Year (which begins October 1 and ends September 30)
GAN	Grant Anticipation Note
GO	General Obligation
IUP	Intended Use Plan
LAC	Legislative Audit Committee
LAD	Legislative Audit Division
LOC	Letter of Credit
MBE	Minority Business Enterprises
MPDES	Montana Pollution Discharge Elimination System
NPS	Nonpoint Source
NMP	National Municipal Policy
PPAD	Planning, Prevention and Assistance Division
PPL	Project Priority List
PWSS	Public Water Supply Supervision
RSID	Rural Special Improvement District
SDWA	Safe Drinking Water Act
SFY	State Fiscal Year (which begins July 1 and ends June 30)
SID	Special Improvement District
SWP	Source Water Protection
TFAB	Technical and Financial Assistance Bureau
TSEP	Treasure State Endowment Program
USDA – RD	United States Department of Agriculture, Rural Development
W_2ASACT	Water, Wastewater and Solid Waste Action Coordinating Team

WBE	Women Business Enterprises
WPCSRF	Water Pollution Control State Revolving Fund